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SUBJECT: ARGENTINA SCENESETTER FOR CODEL GRASSLEY

Classified By: Ambassador Lino Gutierrez for Reasons 1.4 (B) and (D).

Introduction and Summary

¶1. (C) On behalf of Embassy Buenos Aires, I warmly welcome your visit to Argentina on March 23-26. Your visit comes as President Nestor Kirchner continues to consolidate his resounding victory in mid-term legislative elections last October 23. Based on these results, Kirchner has tightened his already firm personal control of political and economic policy. However, Kirchner's performance at the Summit of the Americas last November gained no new friends internationally for Argentina. His explicit criticism of the United States during his Summit speech, and his collaboration with Hugo Chavez and the hard left complicated our bilateral relationship, although recent visits by high-level Congressional and executive branch officials have gone well. Argentina is also seeking to consolidate its impressive economic recovery from the 2001-2002 crises. Argentina will need to lower its inflation rate and increase investment to sustain high rates of growth, lower unemployment and reduce poverty. The two most important issues that affect the bilateral agricultural relationship are Monsanto's ongoing struggle to collect royalties on the use of Round-Up Ready soybean technology and the GOA's recent decision to prohibit the export of fresh and cooked beef for 180 days. As a member of the UN Security Council, Argentina has worked closely with us on issues such as UN reform, counterterrorism, non-proliferation, counternarcotics, and regional issues such as peacekeeping in Haiti. End Summary.

Background

¶2. (C) Argentina was once one of the richest countries of the Hemisphere, achieving a GNP per capita that was among the highest in the world in the early 20th century. However, the history of Argentina over the last 70 years has been one of economic decline and political instability. Many Argentines are at a loss to explain how their country, blessed with rich natural resources, a fertile land and manageable population numbers, could have fallen so far. Some blame the military

dictatorships, which controlled events from 1930-1983; others blame Peron and "Peronism"; and a significant number blame external factors: the IMF, the U.S., and, to a lesser extent, Europe. Gone are the "carnal relations" with the U.S. when Argentina stood out as one of the top U.S. allies in the world during the administration of former President Carlos Menem in the 1990s. The 2001-2002 economic crisis, the worst in Argentine history, changed all that. The election of left-wing Peronist Nestor Kirchner in 2003 marked a different approach in Argentine foreign policy, aligning Argentina more closely to Brazil, MERCOSUR, and Venezuela. That said, Kirchner has cooperated closely with the U.S. on a number of issues, including counterterrorism, non-proliferation and counternarcotics, and regional issues like Bolivia and Haiti.

Political Landscape

¶3. (SBU) President Kirchner won a major victory in the October 23 legislative and provincial elections, receiving a strengthened mandate and beating out his rivals for control of the ruling Peronist Party (PJ). Since then, he has consolidated his political gains with new cabinet appointments and with a controversial move that effectively increased executive branch control over the judiciary. Kirchner is politically strong at home and faces a weak and divided opposition. Argentines give Kirchner much of the credit for the country's Phoenix-like recovery from its 2001-2002 economic crisis, an event equivalent to our Great Depression. His already high approval ratings climbed last year after the conclusion of an audacious debt exchange offer.

¶4. (C) Kirchner revels in a confrontational style, and is quick to pick public fights with business leaders, foreign officials, the Catholic Church, his own military, and political opponents. Two examples last year are illustrative. In the aftermath of a drug scandal at the international airport in Buenos Aires, Kirchner fired virtually every senior general in the Air Force (which was responsible for maintaining airport security) for failing to inform him of the ongoing investigation until five months after it had begun. Kirchner also called for a national boycott of Shell Oil gas stations because of price hikes at the pump. Groups of unemployed workers loyal to Kirchner promptly blockaded Shell gas stations across the country, causing a 70 percent drop in sales. Kirchner later called Shell "among the worst companies in the world."

Argentina Fumbles Summit of the Americas

¶5. (C) President Kirchner's performance at the November 4-5 Mar del Plata Summit of the Americas gained no new friends for Argentina. As chairman of the Summit deliberations, he forged disunity where consensus might have been possible. On the plus side, we reached our essential Summit goals in the Declaration and Plan of Action and 29 of the 34 Heads of State present voiced support for the launch of FTAA negotiations. However, Kirchner's obsessive focus on the International Monetary Fund in his meeting with President Bush, his direct criticism of the United States during his Summit speech, and his collaboration with Hugo Chavez and the hard left complicated our bilateral relationship. Nevertheless, we do not expect Kirchner's undiplomatic public posturing in Mar del Plata to affect the excellent cooperation we continue to receive from Argentina on the key issues of counterterrorism, non-proliferation, and counternarcotics. By January, Kirchner was attempting to make amends. He met with A/S Tom Shannon and pledged Argentina's continued cooperation, particularly on Bolivia and Haiti. Shannon also had positive meetings with all of the new cabinet appointments, restoring the bilateral relationship and focusing on an active bilateral agenda in ¶2006.

Economic Situation

¶6. (U) Argentina has had an impressive economic recovery since suffering the worst economic crisis in its history -- including the largest sovereign default in history and a major devaluation of its currency -- in 2001-02. An export-led boom triggered an 8.8 percent surge in real GDP in 2003, 9 percent in 2004, 9.1 percent in 2005, and a projected 6.9 percent in 2006. The Kirchner Administration has ably managed the nation's public finances and achieved large budget surpluses. Investment increased to 19.5 percent of GDP in 2005, and is projected to increase to 20.8 percent in 2006, but still is below the GOA's target. Unemployment declined to 10.1 percent in the fourth quarter of 2005, but has not fallen as fast as the economy is growing, largely due to a slower recovery in the services sector. Poverty has also fallen from the post-crisis level of 54 percent, but remains stubbornly high. During the first half of 2005, 38.5 percent of the population was living below the official poverty line and 13.6 percent was considered destitute.

¶7. (U) Argentina's robust economic recovery is the result of major economic reforms in the 1990s, the adoption of a market-based exchange rate regime in early 2002, and the combination of strong world economic growth, high commodity prices and low interest rates. Argentina should continue to perform well in 2006, but will need to lower its inflation rate (6.1 percent in 2004, 12.3 percent in 2005, and a projected 12.9 percent in 2006) and increase investment to sustain high rates of growth, lower unemployment and reduce poverty. The short-term success of the GOA's anti-inflation efforts may have a long-term negative impact on the GOA's ability to attract investment. Argentina negotiated a debt exchange in 2005 with 76 percent of its private creditors that offered just over thirty cents on the dollar. Argentina canceled its debt with the IMF on January 3, 2006 by using 40 percent of its reserves to repay the nearly USD 10 billion it owed to the Fund. The Central Bank is now in the process of purchasing dollars to restore its international reserves to earlier levels.

Agricultural Issues

¶8. (U) The agricultural, livestock, and food processing sectors are mainstays of the Argentine economy. Over 50 percent of total export revenue is derived from these sectors, and their direct and indirect contribution to Gross Domestic Product (GDP) and total employment exceeds 25 percent, respectively. Rather than pursuing policies which have fostered wealth creation, the GOA has historically exploited these sectors to cross-subsidize industry, or to support social programs. To that end, the Kirchner administration taxes all agricultural and livestock exports. As examples, the Kirchner Administration taxes soybean exports at the rate of 23.5 percent, and 15 percent for fresh and cooked beef exports.

¶9. (U) The two most important issues that affect the bilateral agricultural relationship are Monsanto's ongoing struggle to collect royalties on the use of Round-Up Ready soybean technology and the GOA's recently implemented measure to prohibit the export of fresh and cooked beef for 180 days.

The crux of the Monsanto issue is the sale of illegal Round-Up Ready (RR) soybean seed by farmers (Monsanto estimates that over 80 percent of the land planted to soybeans is done so illegally by growers who have not paid any royalties for the use of the technology. The GOA does not appear to have the wherewithal nor the will to enforce royalty collections. In the interim, Monsanto has been stopping some shipments of Argentine soybeans in European countries where it has patent protection (it does not have patent protection in Argentina), and has been filing lawsuits to collect the royalties. With the bulk of the soybean harvest about to come on line, this issue will soon be coming

to a head.

¶10. (U) With regard to fresh and cooked beef, the GOA has just implemented a resolution, which prohibits the export of those products for 180 days with the exception of exports to the European Union under the Hilton Quota (28,000 tons), and those to several other countries with which formal bilateral agreements have been established (e.g., Venezuela). This measure has affected negatively at least two U.S. companies that have operations or representation in Argentina, Cargill and Conagra. The GOA believes that through this measure, it will be able to increase the domestic beef supply, which will, in turn, put downward pressure on domestic beef prices, which have been rising rapidly. Given that Argentina's per capita consumption of beef is the highest in the world (over 130 pounds), the price of beef carries significant weight in the calculation of inflation, which the GOA currently deems to be its number one economic concern (the GOA does not want inflation to exceed the 2005 inflation rate of 12.3 percent).

The GOA does not seem to be concerned about the international fallout from this prohibition (broken contracts, market losses, etc.), nor the damage that it will do to Argentina's image abroad. President Kirchner has threatened to extend the ban to a full year if domestic beef prices do not decline. The Embassy has also recently heard reports that the GOA could extend its export ban to dairy products.

Regional Influence

¶11. (C) Argentina has played a positive role in promoting human rights and democratic institutions in the hemisphere, particularly in Haiti and Bolivia. Along with a number of its neighbors, Argentina currently has 575 peacekeeping troops in Haiti in support of MINUSTAH, reflecting its traditionally strong support of UN peacekeeping operations and commitment to Haiti. President Kirchner continues to be a strong supporter of constitutional democracy in Bolivia. Argentina sent a group of election observers to the presidential elections in Bolivia, headed by former Argentine Vice President and current Mercosur President, Carlos "Chacho" Alvarez. President Kirchner told A/S Shannon January 12 that Argentina's policy towards Bolivia mirrors the U.S. policy of constructively engaging the new GOB and steering them in a moderate direction.

¶12. (C) In Venezuela, President Kirchner also played a constructive role in pressing Chavez to hold a recall referendum in 2004 and met with the Venezuelan opposition on two occasions in 2004. More recently, Argentina has sought stronger economic ties with Venezuela. President Kirchner traveled to Puerto Ordaz to meet with Chavez November 22 to discuss a proposed gas pipeline. The GOV also purchased USD 2.8 billion of Argentine public bonds. In January 2005, Argentina assumed a two-year seat on the UN Security Council.

¶13. (U) Argentina's ongoing dispute with Uruguay over the latter's construction of paper mills on the Rio Plata may seriously affect the bilateral relationship and the health of the MERCOSUR customs union. The GOA has refused to remove protestors who are blocking two of the three bridges linking the two countries, interrupting overland transportation from Chile. A recent attempt at a truce between Presidents Kirchner and Vazquez collapsed almost immediately, and opinions have polarized as the blockade enters its seventh week.

Strong on Counter-Terrorism

¶14. (C) Kirchner's administration has strongly supported counter-terrorism policies. The GOA has ratified all of the 12 international counterterrorism conventions. Argentina is a participant in the ThreePlus One regional mechanism, which

focuses on possible terrorist-related activity in the Tri-border region between Argentina, Brazil, and Paraguay. Its border police, federal police, coast guard, and intelligence services provide excellent cooperation on monitoring potential terrorist activity, especially in the Tri-border area. The GOA continues to make efforts to strengthen its Financial Intelligence Unit to combat money launderin and to beef up its National Arms Control Registry (RENAR) in order to get a handle on the production and sale of explosives.

Equally Strong on Non-Proliferation and WMD Interdiction

¶15. (C) In numerous meetings with senior State Department officials, the GOA has voiced strong agreement on almost all of our arms control and nonproliferation objectives. On Iran, the GOA favors a tough line. It voted with the United States at the September 24 IAEA Board of Governors meeting to refer Iran's noncompliance to the UNSC. The GOA is the only South American country to have endorsed the Proliferation Security Initiative (PSI) and has offered to host a PSI exercise. On the IAEA Additional Protocol, the Argentines traditionally have followed the Brazilians, but have indicated that they will eventually sign the AP with or without the Brazilians. Finally, the GOA has implemented the Container Security Initiative (which scans containers for WMD components) and is in the final stages of negotiating an MOU on the Megaports Initiative -- which will passively detect radioactive materials moving through the Buenos Aires seaport -- the first such agreement in South America.

Military-Military Cooperation

¶16. (C) The U.S. military enjoys excellent relations with their Argentine counterparts. Argentine forces participate frequently in exercises with U.S. and regional forces (outside of Argentina) and are currently contributing about 575 troops to the Haiti PKO as well as a significant number of troops to the PKO's in Cyprus and Kosovo. We are stymied, however, by the lack of a political-level agreement on immunities, (i.e., administrative and technical immunities, as defined in the Vienna Convention on Consular Relations, which would be extended to U.S. service members on exercises in Argentina). The lack of this type of agreement precludes many bilateral exercises on Argentine territory. The Argentines unfortunately confuse the immunities issue with Article 98, which deals only with the International Criminal Court. We are looking at a long-term Status of Forces Agreement to resolve these issues.

¶17. (U) To see more Buenos Aires reporting, visit our classified website at: <http://www.state.sgov.gov/p/wha/buenosaires.< /a>>
GUTIERREZ